

S
353.64
L72WS
1977

STATE DOCUMENTS COLLECTION

MAR 1 1978

MONTANA STATE LIBRARY
920 E Lyndale Ave
Helena, Mont 59601

STATE OF MONTANA
WARM SPRINGS STATE HOSPITAL

AUDIT REPORT

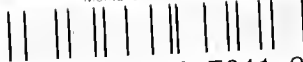
Conducted Under Contract By
Authur Andersen & Co.

June 30, 1977



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MONTANA
STATE CAPITOL • HELENA

Montana State Library



3 0864 1003 7041 3



STATE OF MONTANA
WARM SPRINGS STATE HOSPITAL

AUDIT REPORT

Conducted Under Contract By
Authur Andersen & Co.

June 30, 1977

Digitized by the Internet Archive
in 2010 with funding from
Montana State Library

<http://www.archive.org/details/stateofmontanawa1977mont>

STATE OF MONTANA

Office of the Legislative Auditor

STATE CAPITOL
HELENA, MONTANA 59601
406/449-3122



MORRIS L. BRUSETT
LEGISLATIVE AUDITOR

November 8, 1977

DEPUTY LEGISLATIVE AUDITORS:
JOSEPH J. CALNAN
ADMINISTRATION AND
PROGRAM AUDITS

ELLEN FEAVER
FINANCIAL COMPLIANCE AND
CONTRACTED AUDITS

STAFF LEGAL COUNSEL
JOHN W. NORTHEY

The Legislative Audit Committee
of the Montana State Legislature:

Transmitted herewith is the report on the audit of Warm Springs
State Hospital for the year ended June 30, 1977.

The audit was conducted by Arthur Andersen and Company, Certified
Public Accountants, under a contract between the firm and our office.
The comments and recommendations contained in this report represent the
views of the firm and not necessarily the Legislative Auditor.

The agency's written response to the report recommendations is
included in the back of the audit report.

Respectfully submitted,

A handwritten signature in cursive script that reads "Morris L. Brusett".

Morris L. Brusett, C.P.A.
Legislative Auditor

TABLE OF CONTENTS

	<u>PAGE</u>
General	
Overview	1
Administrative Officials	4
Financial Statements	
Auditors' Report	5
Statement of Assets and Liabilities	7
Statement of Revenues, Expenditures, Encumbrances and Transfers	8
Statement of Changes in Fund Balances	9
Notes to Financial Statements	10
Recommendations for Improvements in Accounting Procedures and Internal Control	18
Prior Year Recommendations	29
Agency Reply	31

WARM SPRINGS STATE HOSPITAL

AUDIT OVERVIEW

SEPTEMBER 15, 1977

Our examination of the financial statements of the Warm Springs State Hospital was conducted primarily to enable us to render an opinion on such statements. However, in conjunction with the examination, we were asked that our procedures include the following:

1. Testing for compliance with all state laws applicable to the Hospital;
2. Examination of the patient deposit fund, which is not recorded in the Statewide Budgeting and Accounting System (SBAS);
3. Examination of payments for capital construction projects administered for the benefit of the Hospital by the Architecture and Engineering Bureau;
4. Examination of transactions with the Warm Springs State Hospital Foundation;
5. Examination of contracts relative to the Community Service program;
6. Examination of grants from the Department of Health, Education, and Welfare and the Department of Labor.

In addition, we were requested to audit fixed asset and inventory records. In the bidder specification it was indicated that accounting records for such items were available (although not recorded in SBAS). As discussed later in our report, the Hospital does not record fixed assets and inventories

of supplies, therefore, the requested work could not be performed. However, the Hospital did physically count certain of its inventories which were recorded on perpetual inventory records (the perpetual inventory records are not integrated with the general ledger). We observed such physical inventory counts and tied the quantities we test counted into the perpetual inventory records. We found no significant differences between the actual count and the perpetual inventory records.

During our examination of the Hospital's financial statements, several items came to our attention which we feel should be considered by the Hospital management and which have been transmitted to them under the title "Recommendations for Improvements in Accounting Procedures and Internal Control." These items were considered by us during our examination; however, they do not modify the opinions expressed in our auditors' reports. The Hospital's actions relating to these suggestions should result in improved procedures and controls in future periods.

In addition to the suggested improvements discussed above certain other items should be brought to your attention:

1. Certain discretionary expenditures, most notably for equipment purchases, did not occur ratably throughout the fiscal year, as one might expect. For instance, approximately 87% of the \$178,000 expended or encumbered for care and custody equipment was expended or encumbered during

June, 1977. Hospital management informed us that equipment purchases are typically delayed until they are certain that appropriations will not be overspent.

2. We were informed by Hospital management that the current appropriation is flexible in that additional funds will be appropriated if the patient load exceeds a specified number, and likewise the appropriation will be reduced if the patient load falls below a certain level. We agree with the Legislature's attempt to introduce more flexibility and control into the appropriation process. The Legislature should continue to develop means to evaluate management. Such evaluations include financial goals such as budgetary control and control of reimbursements and medical goals such as average length of stay, recidivism rates, and success of Community Health Centers.

3. Our "audit contract" called for us to perform an audit in accordance with generally accepted auditing standards and to opine on statements prepared in accordance with the AICPA industry audit guide entitled Audit of State and Local Government Units. Warm Springs State Hospital follows procedures that are not in accordance with generally accepted accounting procedures; thereby creating the situation in which an "adverse opinion" must be rendered by the independent public accountants. In order to avoid this situation it may be advisable to (i) request a "special report" in which the audit procedures to be performed are specifically delineated by the Legislative Audit Committee or the Legislative Auditor. The public accountant would then report that he had completed the specified auditing procedures or (ii) the Legislative Audit Committee specify the accounting principles being followed by the individual agency and require that the independent public accountant report on financial statements prepared in accordance with those specified accounting principles.

ADMINISTRATIVE OFFICIALS
WARM SPRINGS STATE HOSPITAL

Harry C. Xanthopoulos	Superintendent
Richard T. Moore	Administrator
Keith H. Wilson	Fiscal Bureau Chief

ARTHUR ANDERSEN & Co.

BOISE, IDAHO

To the Legislative Audit Committee
of the Montana State Legislature:

We have examined the statement of assets and liabilities of the Warm Springs State Hospital (the "Hospital", herein), an agency of the State of Montana, as of June 30, 1977, and the related statements of revenues, expenditures, encumbrances and transfers and changes in fund balance for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances, except as explained in the following paragraph.

As discussed in Note 1 to the financial statements, certain of the transactions recorded in the Hospital's accounts are initiated by agencies of the State of Montana other than the Hospital. Our examination was therefore limited to the amounts recorded in the accounts of the Hospital and to such underlying documentary support as was available at the Hospital.

As more fully explained in Note 1 to the financial statements, the Hospital follows certain accounting practices which are not in accordance with generally accepted accounting principles. These practices, the effect of which cannot be reasonably determined, include; (i) failure to record fixed assets and inventories of supplies and proper charging of the cost of such items to operations, (ii) failure to distinguish between accounts payable, accrued liabilities, and encumbrances, (iii) failure to record vested accrued employee vacation and sick pay expense, and (iv) failure to utilize inter-fund receivables and payables to record transactions affecting more than one fund.

As more fully explained in Note 3, the Hospital has not recorded certain adjustments as of June 30, 1977. Had these adjustments been recorded, accrued liabilities and expenditures would have increased in the general fund by \$116,256. In the insurance fund, receivable from the Department of Architecture and Engineering would have been reduced to zero and expenditures increased by \$79,896.

ARTHUR ANDERSEN & CO.

Because of the significance of the matters discussed in the preceding paragraphs, it is our opinion that the accompanying financial statements cannot and do not present fairly the financial position of the Warm Springs State Hospital as of June 30, 1977, or the results of its operations and changes in fund balances for the year then ended, in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN & CO.

Boise, Idaho,
September 15, 1977.

WARM SPRINGS STATE HOSPITAL

STATEMENT OF ASSETS AND LIABILITIES

AS OF JUNE 30, 1977

ASSETS					LIABILITIES AND FUND BALANCES				
	General Fund	Federal Grants Fund	Canteen Fund	Insurance Fund		General Fund	Federal Grants Fund	Canteen Fund	Insurance Fund
Cash in State Treasury (Note 1)	\$ 46,462	\$6,678	\$4,685	\$15,235	Accrued expenditures and encumbrances	\$756,436	\$ 391	\$3,830	\$ -
Other cash	3,005	-	-	-					
Appropriation authority available to pay accrued expenditures (Note 1)	756,436	-	-	-	Liability to State Treasury for cash and advances (Note 1)	50,816	-	-	-
Miscellaneous receivables	1,349	-	-	-	Fund balance (Note 1)	-	6,287	855	95,131
Receivable from the Department of Architecture and Engineering	-	-	-	79,896					
	-----	-----	-----	-----		-----	-----	-----	-----
	\$807,252	\$6,678	\$4,685	\$95,131		\$807,252	\$6,678	\$4,685	\$95,131
	=====	=====	=====	=====		=====	=====	=====	=====

The accompanying notes are an integral part of these financial statements.

WARM SPRINGS STATE HOSPITAL

STATEMENT OF REVENUES, EXPENDITURES, ENCUMBRANCES AND TRANSFERS
FOR THE YEAR ENDED JUNE 30, 1977

	General Fund			Federal Grants Fund			Canteen Fund			Insurance Fund		
	Final Budget	Actual	Over (Under) Budget	Final Budget	Actual	Over (Under) Budget	Final Budget	Actual	Over (Under) Budget	Final Budget	Actual	Over (Under) Budget
REVENUES:												
Sale of merchandise	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$220,000	\$127,998	\$ (92,002)	\$ -	\$ -	\$ -
Grant revenue	-	-	-	187,438	135,473	(51,965)	-	-	-	-	-	-
Rental revenue	55,500	56,953	1,453	-	-	-	-	-	-	-	-	-
Insurance proceeds	-	-	-	-	-	-	-	-	-	-	2,517	2,517
Miscellaneous (Note 1)	2,000	779	(1,221)	-	(687)	(687)	-	-	-	-	-	-
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
Total revenues	57,500	57,732	232	187,438	134,786	(52,652)	220,000	127,998	(92,002)	-	2,517	2,517
TRANSFERS FROM STATE TREASURY	15,142,918	15,142,918	-	-	-	-	-	-	-	-	-	-
INTERFUND TRANSFERS	-	2,208	2,208	-	-	-	-	-	-	-	(2,208)	(2,208)
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
Total revenues and transfers	15,200,418	15,202,858	2,440	187,438	134,786	(52,652)	220,000	127,998	(92,002)	-	309	309
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
EXPENDITURES AND ENCUMBRANCES:												
Administration	1,183,699	1,150,312	(33,387)	-	-	-	-	-	-	-	-	-
Care and custody	10,664,585	9,616,044	(1,048,541)	39,000	17,419	(21,581)	-	-	-	-	-	-
Developmental services	2,133,224	1,826,053	(307,171)	185,925	116,207	(69,718)	-	-	-	-	-	-
Community services	1,161,410	1,023,310	(138,100)	-	-	-	-	-	-	-	-	-
Center and recreation hall	-	-	-	-	-	-	298,454	128,839	(169,615)	-	-	-
Insurance proceeds expended	-	-	-	-	-	-	-	-	-	-	15,563	15,563
Other (Note 1)	-	(237,266)	(237,266)	-	10,863	10,863	-	284	284	-	-	-
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
Total expenditures and encumbrances	15,142,918	13,378,453	(1,764,465)	224,925	144,489	(80,436)	298,454	129,123	(169,331)	-	15,563	15,563
TRANSFERS TO STATE TREASURY (Note 1)	57,500	1,824,405	1,766,905	-	-	-	-	-	-	-	-	-
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
Total expenditures, encumbrances and transfers	15,200,418	15,202,858	2,440	224,925	144,489	(80,436)	298,454	129,123	(169,331)	-	15,563	15,563
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
EXCESS (DEFICIENCY) OF REVENUES AND TRANSFERS OVER EXPENDITURES, ENCUMBRANCES AND TRANSFERS	\$ - =====	\$ - =====	\$ - =====	\$(37,487) =====	\$ (9,703) =====	\$ 27,784 =====	\$(78,454) =====	\$ (1,125) =====	\$ 77,329 =====	\$ - =====	\$(15,254) =====	\$(15,254) =====

The accompanying notes are an integral part of these financial statements.

WARM SPRINGS STATE HOSPITAL

STATEMENT OF CHANGES IN FUND BALANCE

FOR THE YEAR ENDED JUNE 30, 1977

	General Fund	Federal Grants Fund	Canteen Fund	Insurance Fund
Fund balance, beginning of year, as reported	\$761,511	\$15,990	\$1,980	\$155,385
Adjustments to conform with generally accepted accounting principles (Note 1)	(761,511)	-	-	-
Excess (deficiency) of revenues and transfers over expenditures, encumbrances and transfers	-	(9,703)	(1,125)	(15,254)
Transfer to the Department of Architecture and Engineering (Note 4)	-	-	-	(45,000)
Fund balance, end of year	-----	-----	-----	-----
	\$ -	\$ 6,287	\$ 855	\$ 95,131
	=====	=====	=====	=====

The accompanying notes are an integral part of these financial statements.

WARM SPRINGS STATE HOSPITAL

NOTES TO FINANCIAL STATEMENTS

AS OF JUNE 30, 1977

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Comparability of Financial Statements

The financial statements included herewith are not comparable in certain respects with previously published financial statements because of more complete adherence to the recommendations of the AICPA Audit Guide for Audits of State and Local Governmental Units.

Basis of Accounting

Inventories of Supplies - The Hospital maintains significant amounts of medical and surgical supplies, pharmaceuticals, food, clothing for patients, and other miscellaneous items. The exact amounts of such supplies are unknown, as the Hospital charges all expenditures for such items to expense as purchased. This accounting treatment is not in accordance with generally accepted accounting principles.

Land, Buildings, and Equipment - The Hospital has significant amounts of land, buildings, and equipment used in the housing and treatment of patients, as well as in the administration of agency activities. The expenditures for such land, buildings, and equipment are charged to expense at acquisition, which is not in accordance with generally accepted accounting principles.

Interfund Accounting - Principles of fund accounting require that each fund within the Hospital be treated as a separate entity. As separate entities, each fund would be charged for all and only its expenditures. Any expenditures by one fund for the benefit of another fund would be recorded as a receivable by the expending fund and payable by the benefiting fund. The Hospital does not record such inter-fund receivables and payables.

Payables, Accruals and Encumbrances - The Hospital does not distinguish among accounts payable, accrued liabilities, and encumbrances. Accounts payable and accrued liabilities represent actual or estimated amounts payable. Encumbrances are obligations in the form of purchase orders or contracts.

They cease to be encumbrances when the goods or services are received and a liability established. Thus, the amount shown as accrued expenditures and encumbrances in the accompanying statement of assets and liabilities represents the total of all these.

Vacation and sick pay accumulated by employees but not yet taken by them is not accrued by the Hospital. Vacation and sick pay vests with the employees and, therefore, should be recorded in the accounts. The amount of this liability is not known, but is potentially significant.

Reversions - Any general fund state appropriations unexpended or unaccrued by fiscal year-end revert back to the state. Therefore, a liability to the state for all general fund assets is shown. A receivable from the state for funds to pay accrued liabilities is also established and therefore the fund balance has a zero balance. Normally, Cash in Treasury has no balance at year-end. A balance is shown on the statements because the state allowed the Hospital to record expenditures made on July 1, 1977, as fiscal year 1977 expenditures. These expenditures were reclassified.

Prior Year Expenditure and Revenue Adjustments - These accounts include revenue and expense that apply to the previous year that were not accrued at year-end. They are included in Miscellaneous revenue and Other expenditures.

Description of Funds

General Fund - The general fund is used primarily to account for operations of the Hospital that are funded through state appropriations, such as the care and custody of patients, developmental treatment, and administration. Miscellaneous revenues, such as housing rent, are also included in the general fund.

Federal Grants Fund - Monies received from federal grants and the expenditures made against them are recorded in the federal grants fund. Expenditures consist largely of salaries, but include other items allowed under the grant.

Insurance Fund - The insurance fund is used to account for receipt of insurance proceeds and the subsequent expenditure of those proceeds. After two years, unexpended proceeds are transferred to the general fund.

Canteen Fund - The operations of the canteen and recreation hall located on the Hospital grounds are accounted for in a separate fund. Receipts consist of income derived from the sale of food. The cost of the food and its preparation and serving are included in expenditures of the canteen fund except for food that is obtained from the Hospital cafeteria food inventory.

Transactions Initiated by Other Agencies - Certain other state agencies frequently access the Hospital's accounting system. Payroll transactions, fund balance transactions, and closing entries are made by other agencies. Documentary support for those transactions is sometimes unavailable to the Hospital.

2. PATIENT FUNDS

Description - The Hospital acts as custodian for patients' monies. Such monies are deposited in a non-state treasury bank account called the patient deposit account. If a patient has more cash than is necessary to meet short-term needs, the excess is deposited in an individual savings account in his name. Balances in the patient accounts are summarized below:

<u>ASSETS</u>		<u>LIABILITIES</u>	
Cash	\$161,660	Patient fund-operating	\$144,462
		Patient funds-savings	12,966
		Unredeemed canteen coupons	4,232
	-----		-----
	\$161,660		\$161,660
	=====		=====

These balances are not included on the Hospital's financial statements.

3. AUDIT ADJUSTMENTS

Certain material audit adjustments were not booked by the Hospital.

General Fund

Certain liabilities relating to fiscal year 1977 were not accrued. This adjustment would have increased accrued liabilities by \$116,256. Expenditures were increased as follows: Community Services by \$86,799, Care and Custody by \$18,357, and Developmental Services by \$11,100.

The effect of these adjustments on the financial statements
is summarized below:

STATEMENT OF GENERAL FUND

ASSETS AND LIABILITIES

	<u>AS REPORTED</u>	<u>WITH ADJUSTMENTS</u>
ASSETS:		
Cash in state treasury	\$ 46,462	\$ 46,462
Other cash	3,005	3,005
Appropriation authority available to pay accrued expenditures	756,436	872,692
Miscellaneous receivables	1,349	1,349
	-----	-----
	\$807,252	\$923,508
	=====	=====
LIABILITIES AND FUND BALANCE:		
Accrued expenditures and encumbrances	\$756,436	\$872,692
Liability to state treasury for cash and advances	50,816	50,816
Fund balance	-	-
	-----	-----
	\$807,252	\$923,508
	=====	=====

STATEMENT OF GENERAL FUND REVENUES, EXPENDITURES,
ENCUMBRANCES AND TRANSFERS

	<u>AS REPORTED</u>	<u>WITH ADJUSTMENTS</u>
Total revenues and transfers	\$15,202,858	\$15,202,858
EXPENDITURES AND ENCUMBRANCES:		
Administration	\$ 1,150,312	\$ 1,150,312
Care and custody	9,616,044	9,634,401
Developmental services	1,826,053	1,837,153
Community services	1,023,310	1,110,109
Other	(237,266)	(237,266)
	-----	-----
Total	\$13,378,453	\$13,494,709
Transfers to state treasury	1,824,405	1,708,149
	-----	-----
Total expenditures, encumbrances, and transfers	\$15,202,858	\$15,202,858
	-----	-----
Excess (deficiency) of revenues and transfers over expenditures, encumbrances, and transfers	\$ -0-	\$ -0-
	=====	=====

Insurance Fund

Most expenditures for construction during fiscal year 1977 were not recorded until the following year. The adjustment increased expenditures and reduced transfers to construction in progress by \$79,896.

The effect of this adjustment on the financial statements is as follows:

STATEMENT OF INSURANCE FUND ASSETS AND LIABILITIES

	<u>AS REPORTED</u>	<u>WITH ADJUSTMENTS</u>
ASSETS:		
Cash in state treasury	\$15,235	\$15,235
Transfer to construction in progress account	79,896	-
	-----	-----
	\$95,131	\$15,235
	=====	=====
 LIABILITIES AND FUND BALANCE:		
Fund balance	\$95,131	\$15,235
	-----	-----
	\$95,131	\$15,235
	=====	=====

STATEMENT OF INSURANCE FUND REVENUES, EXPENDITURES,
ENCUMBRANCES, AND TRANSFERS

	<u>AS REPORTED</u>	<u>WITH ADJUSTMENTS</u>
Total revenues and transfers	\$ 309 -----	\$ 309 -----
EXPENDITURES AND ENCUMBRANCES:		
Insurance proceeds expended	15,563	95,459
Transfers to state treasury	- -----	- -----
Total expenditures, encumbrances, and transfers	\$ 15,563 -----	\$ 95,459 -----
Excess (deficiency) of revenues and transfers over expenditures, encumbrances, and transfers	\$(15,254) =====	\$(95,150) =====

4. TRANSFERS TO THE DEPARTMENT OF ARCHITECTURE
AND ENGINEERING:

The Department of Architecture and Engineering handles construction projects for all state agencies. Any funds appropriated to the Hospital that are transferred to the Department for construction are recorded in the "Transfer to Construction in Progress" accounts (referred to as "Receivable from the Department of Architecture and Engineering" on the Statement of Assets and Liabilities). During fiscal year 1977, \$45,000 was reappropriated from the Hospital's construction in progress account to the Department of Architecture and Engineering. The money is recorded by the Department, but will be used for Hospital construction projects.

5. DONATIONS FOR SPECIFIED PATIENT PURPOSES:

The Hospital acts as custodian over donations received for specified patient purposes. All amounts recorded in the "Donations fund" are considered to be payable to the patient purpose specified by the applicable donor. At June 30, 1977, the cash balance in this account totaled \$2,134. The balances in this account are not included in the Hospital's financial statements.

•

WARM SPRINGS STATE HOSPITAL
=====

MEMORANDUM OF SUGGESTIONS ON
ACCOUNTING PROCEDURES AND
INTERNAL CONTROL

Boise, Idaho,
September 15, 1977.

ARTHUR ANDERSEN & Co.

BOISE, IDAHO

To the Legislative Audit Committee
of the Montana State Legislature:

The accompanying memorandum includes suggestions for improvement of accounting procedures and internal accounting control measures that came to our attention as a result of our examination of the financial statements of the Warm Springs State Hospital for the year ended June 30, 1977. The matters discussed herein were considered by us during our examination and they do not modify the opinion expressed in our auditors' report dated September 15, 1977, on such financial statements.

In accordance with generally accepted auditing standards, we performed a review and evaluation of existing internal accounting controls for the purpose of providing a basis for reliance thereon in determining the nature, timing, and extent of the audit tests applied in connection with our examination of the Hospital's 1977 financial statements. While certain matters which came to our attention during the review are presented in the accompanying memorandum for the consideration of you and Hospital management, such a review was not designed for the purpose of making detailed recommendations and would not necessarily disclose all weaknesses in the existing system.

The accompanying memorandum also includes comments and suggestions with respect to other financial and administrative matters which came to our attention during the course of our examination of the financial statements. These matters are offered as constructive suggestions for the consideration of you and Hospital management as part of the ongoing process of modifying and improving accounting control and other financial and administrative practices and procedures.

Very truly yours,

ARTHUR ANDERSEN & CO.

Generally Accepted
Accounting Principles

In preparing its financial statements, the Hospital has applied certain policies and principles which are not in accordance with generally accepted accounting principles and, therefore, the financial statements do not fairly present the financial position of the Hospital and the results of its operations. The policies and principles in question are as follows:

1. Fixed assets and inventories are not recorded in the general ledger. These items represent a significant portion of the Hospital's assets. We recommend these assets be physically counted and recorded at their cost. The cost of the fixed assets should be depreciated over the estimated useful life of the assets. The cost of the inventories should be charged to operations as they are consumed.

2. No distinction is made in the general ledger between accounts payable, accrued liabilities, and encumbrances. Encumbrances are obligations in the form of purchase orders or contracts. They cease to be encumbrances when the goods or services are received and a liability established. The purpose of encumbrances is to reserve a portion of an appropriation. They are not liabilities; whereas, accounts payable and accrued liabilities represent actual or estimated amounts payable. We recommend these items be segregated in the general ledger accounts.

3. Vacation and sick pay accumulated by employees but not yet taken by them was not accrued by Warm Springs. Vacation and sick pay vests with the employees and, therefore, should be recorded in the accounts. The amount of this liability is not known but is potentially significant.

4. The Hospital carries all grants in a separate fund. If a grant has been approved, but the money has not been received, expenditures against the grant are charged to the general fund. When the cash is received, the expense is transferred to the grant fund. These transactions should be recorded by using inter-fund receivables and payables.

Purchasing Procedures -
State of Montana

As specified by the State of Montana,
all purchases of items over \$150,
except for items such as utilities (for which the approval is
made annually), are to be made by the State Purchasing Department.
Accordingly, all clothing, food, medical equipment, supplies, and
pharmaceuticals are purchased through the State Purchasing Depart-
ment.

Conceptually, the system of centralized purchasing
should allow all state agencies to obtain needed goods and
services at the lowest possible price. However, in the case
of certain clothing, medical and pharmaceutical purchases, the
equally important objective of purchasing the "correct" goods
is not achieved or is made difficult to achieve where special
expertise is required to properly solicit and evaluate bids.
Using the example of medical and pharmaceutical purchases, the
appropriate Hospital employee is generally more able to evaluate
the product he is buying and should, therefore, have final
authority in effecting the purchase.

In addition, there appears to be a significant amount
of communication and follow-up required to effect purchases of
goods having specified quality characteristics (principally
certain clothing and medical supply purchases). Because of this,
the State Purchasing Department purchases such items infrequently

requiring orders for large quantities. This type of practice has the undersirable effect of causing unnecessary inventory build-up and significantly increasing the risk of obsolescence and spoilage.

We recommend that the centralized purchasing procedures as they relate to unique items be reviewed and a more practical purchasing system be developed for such purchases. Much of the benefit of controlled purchasing for these items can still be retained through budgetary control.

Purchasing Procedures -
Warm Springs State Hospital

At the Hospital, all purchase requisitions, prepared by appropriate department supervisors, are examined by the business office before preparation of a purchase order. The business office determines that the funds are available for the purchase by examination of the appropriation before routing the requisition to the Hospital purchasing department for preparation of the purchase order. Once the purchase order has been prepared, it is returned again to the business office for review and approval.

This resubmission of the purchase order to the business office appears to be unnecessary because the business office has already approved the requisition. We recommend that it be eliminated to avoid the delay and cost involved. Documentation of the approvals can be made on the requisition form.

Purchasing Procedures -
Other

Purchase requests are made through requisitions by an individual in the requesting department. Presently some individuals indicate on the requisition which account and program should be charged. To assist the business office in processing requisitions and to avoid confusion, we suggest that all departments indicate the appropriate account and program numbers on requisitions.

The Hospital does not maintain formal price lists from its vendors (i.e., those used by the Hospital for purchases under \$150). Purchasing efficiency would be improved if competitive price lists were maintained and used.

Medicaid and Medicare
Reimbursements

As a part of its report on the examination of the financial statements of Warm Springs State Hospital as of June 30, 1974, the State of Montana Legislative Auditors' office discussed the situation whereby Medicaid and Medicare reimbursements are recorded by the Department of Institutions rather than the institution performing the service. The Legislative Auditor recommended that such reimbursements be recorded by the institutions. We agree with this recommendation, with the following modifications.

Presently, the personnel involved in the reimbursement process, such as those who prepare Medicare billings, are

employees of the Department of Institutions, rather than Warm Springs State Hospital. Yet, all of the information required for their duties is generated by Hospital employees. Since much of the information required by third party payors is of no value to the Hospital (since it is not the recipient of the resulting reimbursement), there is no incentive for Hospital employees to routinely gather the data necessary to properly control reimbursements. As a result, the Hospital cannot control the persons obtaining the reimbursement, and the persons obtaining the reimbursement cannot control the data flow from the Hospital. Therefore, no one knows whether or not the State is receiving maximum reimbursement. Since the scope of our audit did not include an examination of the financial statements of the Department of Institutions, we were not able to ascertain whether or not the Legislative Auditor's aforementioned recommendations as they pertain to that Department have been implemented.

We recommend that the Hospital be given control over the collection of the reimbursements. As such, persons presently involved in the reimbursement process should become Hospital employees, reporting to the fiscal bureau chief. The Hospital's annual budget should include estimated reimbursements, and significant variances therefrom should be adequately investigated, explained and corrective action taken where needed.

Inventory The Hospital is currently in the process of entering all items of inventory on a Supplies Inventory Management System (SIMS). This is a computerized, perpetual inventory system. Inventory is not recorded on the books, so the primary purpose of the system is for inventory control and re-order. Prior to the use of SIMS, a hand prepared perpetual inventory system was used.

Most purchases of inventory are made semi-annually or quarterly. At the time of purchase, a physical inventory is taken to determine quantities on hand and quantities needed.

We do not believe that such a complex inventory system is necessary at the Hospital. The volume of activity in the inventories is small. In addition, a physical inventory is taken prior to placing each order. The cost of using SIMS is estimated by Hospital employees to be about \$7,000 per year for programming, data processing, and rent. We recommend that the Hospital reevaluate the system and determine if it is cost justified.

Integrity of Accounting
System

The Department of Administration frequently accesses the Hospital's accounting systems and in many cases does so without notifying the Hospital. Payroll entries, both regular and accrual, fund balance entries, and closing entries are made by that Department.

The integrity of the Hospital's accounting system has been impaired by this situation because the possibility of errors is increased due to the additional communication required. During fiscal year 1977, for example, that Department established a continuing appropriation which the Hospital did not request. In addition, support for entries is sometimes not available to the Hospital. For example, methods used by the Department for determining year-end payroll accruals could not be explained by Hospital employees.

We recommend that the Hospital have complete responsibility of all entries made to its accounts, including obtaining and maintaining adequate supporting documentation for all entries.

<u>Account Distributions</u>	The Hospital records certain non-salary and wage expenses as salaries. Examples are professional fees and payments to the community mental health centers. These expenditures are not salaries or wages and should not be classified as such. We recommend that such non-salary and wage expenses be charged to the contracted services account rather than the salaries and wages account.
----------------------------------	---

<u>Patient Accounts</u>	In his 1974 report, the Montana Legislative Auditor discussed the funds managed for the patients by the Hospital. The following are their recommendations
-------------------------	---

that have not yet been implemented:

It was recommended that the Hospital:

- deposit the patients' accounts in a state treasury account.
- establish an agency fund and record patient accounts in the Statewide Budgeting and Accounting System (SBAS).
- implement adequate separation of duties for processing patient account transactions.
- determine the amount of money necessary for patients' daily needs and invest the remainder in the Investment Division's short-term investment pool.
- dispose of interest earned on patients' monies prior to the establishment of individual savings accounts in accordance with applicable state laws. This interest is currently held in one account and is not designated to any individuals.

In addition, we make the following recommendations concerning patient savings accounts which may be opened if the patient has money in excess of day-to-day needs. These are individual, interest-earning accounts. Interest is not posted to individual accounts until the month following year-end. Thus, if a patient is discharged prior to the posing date, the interest earned is not given to him. That interest is still posted to and carried in his individual account, leaving many accounts with very small balances. We suggest that interest on patient savings accounts be posted on a timely basis. For those patients discharged between year-end and receipt of the bank statement,

the Hospital should call the bank and request the amount of interest earned to date. Account balances would be properly reflected and discharged patients would receive their interest.

Cash Receipts The Hospital maintains a canteen and recreation hall on the grounds for patients and visitors. Cash receipts are stored in a safe each night and deposited weekly. They are posted weekly through collection reports processed by the Accounting Division in Helena. Because receipts are only deposited weekly and there are delays in processing, cash receipts are not always recorded in the proper month.

Other cash receipts are received by Patient Deposit. They consist of rental income, grant revenues, and other miscellaneous receipts. These are deposited semi-monthly at which time a collection report is prepared.

We recommend that all cash receipts be deposited intact daily. The Hospital should prepare the collection reports daily. Posting to cash receipts should be made from the Hospital's collection reports, rather than collection reports from the Accounting Division in Helena.

Payroll The majority of the Hospital's expenditures are payroll or payroll related. As such, much of the Hospital's Internal Control System should, and does, focus on

the payroll system. We noted the following areas that require improvement regarding this system:

1. Personnel Files - Personnel files are not always complete, particularly in the case of long-time employees. Deduction authorizations, current payroll status forms, etc., may be missing from an employee's file. We recommend that an effort be made to "bring current" the existing files, and that a mechanism for systematic update (such as a bi-annual refiling of Form W-4) be instituted.

2. Approval of Time Sheets - Current procedures require the signature of a timekeeper as an approval of hours worked. We recommend as an additional control over departmental payroll expenses that each employee's supervisor also sign the time sheets. The payroll clerk should be instructed not to process time sheets that do not bear the requisite signature (several were noted as being processed with no approval).

WARM SPRINGS STATE HOSPITAL

PRIOR YEAR RECOMMENDATIONS

In the course of our work and by discussion with Hospital personnel, we have reviewed each of the Legislative Auditor's recommendations included in his fiscal 1974 report to determine the present status of compliance with such recommendations. Those recommendations with which the Hospital has not fully complied, along with comments as to the present status of compliance are as follows:

(The page on which the recommendation appears in the Legislative Auditor's 1974 report is indicated in parenthesis).

- The Hospital should comply with state nepotism laws. (Page 14)
There is presently one case of nepotism in the Hospital Laundry.
No further cases were noted.
- The Hospital should separate the payroll preparation and warrant distribution responsibilities. (Page 21)
- The Hospital should budget and charge payroll for janitorial workers to the general services (administrative) program rather than care and custody. (Page 21)
- The Hospital should require written substantiation for extended sick leave and approve sick leave for authorized

purposes only. (Page 24)

This is left to the discretion of department supervisors.

- The Hospital should collect a fee for water and sewage service provided to others. (Page 38)

Management is of the opinion that it would be too expensive to monitor and collect this nominal fee.

- It was recommended that the Hospital use hospital vehicles for patient training rather than the mechanics instructor's personal projects. (Page 57)

This would violate union contracts.

- Internal control over cash receipts from Canteen and Recreation Hall Operations should be improved and personal services and supplies should be accounted for on an actual use basis. (Page 61)

The Hospital continues to subsidize the Canteen.

- Concerning the Foundation, the Hospital should deposit donations in a state treasury account, seek recovery of Hospital money previously given to the foundation, and record in SBAS the receipt and subsequent expenditure of all donations. (Page 67)

The Foundation still exists and controls the disputed donation.

WARM SPRINGS STATE HOSPITAL

AGENCY REPLY

Generally Accepted Accounting Principles

1. Up until now one of the shortcomings of SBAS has been the inability to record fixed assets. The Governmental Accounting Policies Board has just approved a plan to make such recording possible. Therefore in the near future, as soon as the program is operational, fixed assets will be recorded in the accounts. SBAS does not currently have the ability for other than enterprise-type agencies to record inventories. Under the current process the control factor is the appropriation authorized the agency. It is then up to the individual agencies to control their own inventories. W.S.S.H. Management feels that we have a good control system in SIMS.

2. In that encumbrances do not become liabilities until such time as the goods or services are received and the short time period between receipt of merchandise and payment it is not felt that creating the liability on the books would be warranted. The paying of the claims is an ongoing process with payments being made on almost a daily basis. In order to create the liability it would be necessary to process a journal voucher setting it up. Then instead of paying the claim against the encumbrance you would pay it against the liability. It would be possible, due to our short payment period, that you would be paying a claim against a liability that has not been established on SBAS in which case it would reject and you would have to process it again. It would appear that for the most part we would be creating extra work for ourselves. In addition, this does not give us any useful management tool which we do not already have accessible to us through the Encumbrance Detail Register.

3. Central Payroll is currently studying the feasibility and desirability of accruing these benefits. We do concur that these benefits should be recorded in the accounts.

4. Effective immediately we will be using inter-entity receivables and payables when necessary.

Purchasing Procedures

State of Montana

We would concur in this recommendation. We feel that we are more qualified than central purchasing in assessing the best

buy on certain items where exact specifications must be met. By allowing the individual agency to go out and purchase it, it would be possible to obtain smaller quantities thus reducing storage space required as well as assessing whether the products of a particular vendor meet our needs satisfactorily. At the present time we are committed to a particular product until it is used up and with items being ordered on an annual or semi-annual basis we receive a large supply. If they do not meet our needs the way we feel it should, even though it might meet the specifications, we are stuck with the product until it is gone.

Warm Springs State Hospital

The resubmission to the business office is necessary to obtain an authorized signature. At the present time the Fiscal Bureau Chief, Accounting Supervisor, Hospital Administrator and Hospital Superintendent are the only authorized signatures accepted by the Department of Administration. It is not felt by management that we want to vest this authority in a purchasing agent. The delay involved is minimal as the purchasing office and the business office are located in the same building. It is recognized that this was not true during the time of your field examination so there was some delay at that time. It is also felt that the cost is very minimal when compared to the control exercised through a limited number of authorizing signatures on documents.

Other

It has not been until just recently that department managers have been involved deeply with their budgets. During this past fiscal year they were heavily involved in the preparation of their individual budgets for fiscal year 77-78. This involved introducing them to expenditure coding. Up until this time they were not knowledgeable enough about the accounting system to code their own store orders. We presently have some of the department managers who do their own coding and we hope to have all of them doing so by the end of the current fiscal year.

It is felt by Hospital management that it would not be feasible to maintain accurate price lists in view of the often changing prices. Also, with only two employees in the purchasing department it is felt that there would not be sufficient time available. In lieu of price lists we make telephone calls to confirm prices on purchases of less than \$150.00 prior to the purchase order being issued.

Reimbursements

We concur in this recommendation. We have previously recognized this problem and have requested clarification from the Department of Institutions, concerning reimbursements. W.S.S.H. requested approximately 1½ years ago that all of the reimbursement functions come under the responsibility of the Hospital.

At that time a panel of health care experts in the State of Montana visited the institutions to determine what would be best for the reimbursement function. In essence this panel felt it would be more cost effective to centralize the billing and collection effort in Helena, although they did feel that a more in depth study should be conducted prior to doing this. It appears at the present time that all personnel with the exception of two, will be relocated in Helena in the very near future. W.S.S.H. will continue to prepare the required cost reports for Medicare and Medicaid. We do not however, feel that this will result in the best operation as you still have two separate entities responsible for reimbursements with no one knowing if maximum reimbursement is being received.

Inventory

At fiscal year-end we had 3,641 items on SIMS. Since that time we have added office supplies as well as some additional food and clothing items. As of 10-31-77 we have a total of 3,967 items on the system with a total dollar value of \$413,401.90. Of these items 1,895 are everyday working items. Within the next six months we will be adding over 2,000 maintenance items to bring the total items over 6,000.

As a result of this system we have been able to delete a stock clerk position whose responsibility was maintaining a manual inventory system. This position had an annual salary of over \$9,000. The SIMS inventory system is not only cheaper to maintain but it is also a more efficient and accurate system.

Integrity of Accounting System

We concur in this recommendation.

Account Distributions

The reason for charging the Mental Health Center payments to personal services is as follows: It was felt that we were in fact purchasing personal services in the Community. At the time our appropriation was given we had approximately 950 patients in the Hospital and we were appropriated salaries and positions to care for these patients. As the deinstitutionalization program progressed we had fewer patients (approximately 500 at year-end) therefore are required fewer personnel. The patients needs were being met in the community and it was determined that the money should follow the patients. HB 289, appropriation bill for the 1975-1977 biennium, stated that we were committed to spending a certain amount for personal services or revert the amount not so spent. The Office of Budget and Program Planning agreed that payments to the Community Mental Health Centers could be charged to personal services without violating HB 289.

Patient Accounts

In regards to previous recommendations our responses remain unchanged.

We currently do call the bank for interest amounts on a patient's account upon his discharge. Up until the present time they have been giving us only the amount of interest, posted to the particular account. They had not been adding any interest accrued since the last posting date. We have talked with one of the Vice Presidents at the bank and impressed upon him the need for having all interest recorded and withdrawn when the patient is discharged. We have been assured by him that in the future all interest will be recorded when so requested.

Cash Receipts

It is our feeling that depositing the cash on a daily basis would not be cost effective. The amounts of cash received in the Canteen averages about \$120.00 per day with the balance being made up of coupon sales. If we were to deposit daily it would be necessary to write checks daily from patient deposit to the Canteen. In addition, it would require that a teamster be available on a daily basis to take the deposit into town. The time involved for the teamster would likely be an hour plus the fringe benefits and gas. Also, there would not always be a teamster available to make the trip for the deposit. In that the money is stored in a locked safe in the business office it is not felt that there is too much of a chance of the money being stolen or lost.

We will in the future however, make the final month end deposit and collection report at month-end so that the deposits are recorded in the proper month. There still is the possibility however, that it will not be recorded on SBAS for the proper month due to the cut-off dates established by the State Treasurer's Office.

Payroll

1. Personnel Files - As of October 28, 1977, all the personnel files are current with the exception of Form W-4's. To correct the deficiency of missing or outdated Form W-4's such forms will be distributed in the near future with payroll checks to be completed and returned to the Personnel Department.

2. Approval of Time Sheets - In the future it will be required that the timekeeper's supervisor approve all the time sheets. Also, in the near future it should be possible to eliminate the need for submission of time sheets due to the computerized time system which automatically records and accumulates an employee's time. The delay in becoming fully computerized lies in the fact that there is an unlocated programing error in the benefits accumulation program. We have been assured by IBM personnel that this error will be corrected in the near future.

Prior Recommendations

All prior responses remain unchanged.

